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TRANSCRIPT

Q2 2023 Earnings Conference Call

WillScot Mobile Mini Holdings Corp. (Nasdaq: WSC)

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Tim Boswell, President & Chief Financial Officer

Nick Girardi, Sr. Director of Treasury and Investor Relations

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Faiza Alwy, Deutsche Bank

Kevin McVeigh, Credit Suisse

Philip Ng, Jefferies LLC

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Sean Wondrack, Deutsche Bank

Steven Ramsey, Thompson Research Group, LLC

Timothy Mulrooney, William Blair & Company L.L.C.

TRANSCRIPT

Operator

Welcome to the Second Quarter 2023 WillScot Mobile Mini Earnings Conference Call. My name is Amy, and I will be your operator for today's call. Please note that this conference is being recorded.

I will now turn the call over to Nick Girardi, Senior Director of Treasury and Investor Relations. Nick, you may begin.

Nick Girardi

Good morning, and welcome to the WillScot Mobile Mini Second Quarter 2023 Earnings Call. Participants on today's call include Brad Soultz, Chief Executive Officer; and Tim Boswell, President and Chief Financial Officer.

Today's presentation material may be found on the Investor Relations section of the WillScot Mobile Mini website.

Slide 2 contains our safe harbor statement. We will be making forward-looking statements today during the presentation and our Q&A session. Our business and operations are subject to a variety of risks and uncertainties, many of which are beyond our control. As a result, our actual results may differ materially from today's comments. For a more complete description of the factors that could cause actual results to differ and other possible risks, please refer to the safe harbor statement in our presentation and our filings with the SEC.

With that, I'll turn the call over to Brad Soultz.

Brad Soultz

Thanks, Nick. Good morning, everyone, and thank you for joining us today. I'm Brad Soultz, CEO of WillScot Mobile Mini. Let's start on Slide 16 of our 2Q investor deck. 2Q 2023 was another terrific quarter for our company and showcases the predictable compounding returns and cash generation that are clearly accelerating as we scale the business. As shown on this page, we are already exceeding or on track to outpace all of the performance metrics that we laid out in our Investor Day in November of 2021.

Revenue increased 11% year-over-year due to the compounding effect of rate optimization and VAPS penetration. Adjusted EBITDA increased 25% to $261 million and adjusted EBITDA margin expanded 500 basis points, a function of both the high flow-through of rate and VAPS as well as the margin enhancement initiatives on which we've been focused since we began operating on the SAP platform about 2 years ago. At 45% adjusted EBITDA margin, we're at the top-end of the milestone range that we laid out in our Investor Day.

Cash generation in our business is just outstanding. We achieved a company record of $160 million of free cash flow and 27% free cash flow margin during the quarter. Year-to-date, we've delivered $263 million of free cash flow and expect to generate well in excess of $500 million of free cash flow in 2023. Clearly, we're well on our way towards our next free cash flow milestone of $650 million. And with leverage at 3x net debt to adjusted EBITDA and the bottom end of our target range of 3x to 3.5x, our approach to capital allocation remains unchanged and unconstrained. During the quarter, we allocated $43 million to net CapEx. We invested $70 million in M&A, and we repurchased 5.4 million shares of our common stock for $239 million. Over the last 12 months, we've now returned $891 million to

shareholders and reduced economic share count by 9.1%. All in, our financial performance was outstanding, and our results this quarter demonstrate the powerful and predictable compounding of our portfolio.

Commercially, I'm excited to announce that our team successfully launched our premium storage VAPS offering, or PRORACK, which you can see a picture of on the cover of this investor deck or on our website. PRORACK is a proprietary space management solution that fits inside storage containers. It's safe, durable, easy to install, easy to use and solves customer problems with flexible configurations to function as desk, material storage, pipe rack, tool crib, shelves, or any of the above. PRORACK is modular in nature, in that we can connect up to 4 PRORACK modules on each side of a 40-foot container, building flexible configurations for our customers. PRORACK is a perfect example of the type of innovation that differentiates us in the market and helps our customers operate more safely, comfortably, and efficiently during their projects. I'm incredibly proud of the product development, commercial, and operational teams and the collaboration that drove this innovation as well as many others in the pipeline.

As a reminder, VAPS across the portfolio represents $500 million of our $1 billion of idiosyncratic growth levers. Modular, including the ground level offices, represents $370 million to the $500 million based on the portfolio currently in place. In order to realize the balance of the $130 million from Storage, we simply need to achieve storage VAPS delivered rates of $70 per unit. We're extremely confident in reaching and likely eclipsing this milestone in the next 3 to 5 years. As a point of reference, our last 12-month delivered rate in storage is already over $20 per unit and that's with only 1 year since the rollout of our basic offering and before any contribution from PRORACK.

Flipping back to Slide 10. In short, not much has changed from our Q1 2023 earnings call with respect to end-market demand. We're continuing to experience robust demand across commercial and industrial end markets, particularly in manufacturing and professional services. As expected, retail demand was down in the quarter, driven by deferral of storage remodels at major non-mall-based retailers, which is impacting storage volumes in Q2 and Q3. That said, we've now started to receive orders for seasonal storage needs. And while we're early in, both the timing and quantity of these are consistent with our expectations. Also, as noted and expected, non-residential construction starts, both on a dollar and a square foot basis, has been below the record levels in 2022. The Architectural Billing Index, which has been a good forward indicator of non-residential construction starts in 9 to 12 months, has now stabilized at neutral to positive ranges in the second quarter, following modest contracting levels throughout the prior 2 quarters. And like our customers' project backlogs, the AIA, the inquiry index leading to the ABI has remained robust throughout. Further of note, our second quarter quoting activity in the NA Modular segment was up modestly in the second quarter, again against extremely robust levels realized in 2022.

Geographically, strength in the U.S. Southeast from Carolinas down to Florida, the Midwest and the desert states have been countering relatively weaker demand in the U.S. Northeast, U.S. West Coast states and Canada. And while we continue to maintain a prudent outlook with respect to end market demand through the balance of 2023, we're extremely excited about the potential tailwinds associated with onshoring and reshoring and infrastructure projects that we expect to further accelerate in 2024 and persist for years to come. Large-scale reshoring projects have already been breaking ground in North America, which represent material and long-duration opportunities to deploy our services. We're actively participating, bidding and winning multiple billion-dollar projects in sectors such as chemicals, power gen, renewables, electric vehicles, semiconductors, et cetera. And with our recently combined CRM, our storage and modular field sales teams now have uniform visibility into all projects, and we are even further disproportionately well positioned to provide complex value-added total space solutions to our customers with our unrivaled scale, product offering, capabilities, and particularly as the project size and complexity increase.

And quickly on Slide 18. Our rates continued to compound powerfully and predictably across the portfolio. In our Storage segment, portable storage average monthly rates increased 27% as we continue to execute our price management roadmap, leverage our best-in-class tools and technology investments and the new product positioning. Storage VAPS, while still in the very early innings, will begin to contribute more meaningfully in 2024 and provide a recipe for years of sustained double-digit rate growth as we've experienced over the last 5 years in the Modular segment. In our Modular segment, rental rates increased 19% versus prior year and a robust 6% sequentially, driven by both increased rate and VAPS penetration. Spreads between modular delivered spot rates over the last 12 months and the average of the portfolio continue to remain above 30%.

Now before I hand the call over to Tim, I would like to take a moment to thank our team for safely and frugally delivering yet another outstanding quarter and progressing each of our $1 billion idiosyncratic growth levers. Along the way, the team has exceeded or is on track to eclipse all 7 of the ambitious multiyear growth and return metrics we committed to at our Investor Day in late 2021.

With that, I'll hand the call over to Tim for additional context.

Tim Boswell

Thank you, Brad, and good morning, everyone. Page 21 shows a high-level summary of the quarter. Similar to Q1, we saw exceptionally strong financial performance across both segments, driven by continued strong pricing and value-added products penetration and outstanding margin performance across all revenue streams, resulting in record profitability and free cash flow. As Brad pointed out, we are approaching or exceeding every key financial metric in our operating ranges that we set forth at our Investor Day back in 2021. We still see over $1 billion of opportunity across our 5 growth levers. So as we look ahead into 2024, it's logical to expect that we'll find upside across many of these ranges.

In the immediate term, the business is performing exactly as we would expect in this environment. Leasing revenues are compounding powerfully up 16% year-over-year, driven by pricing and value-added products, which given our 3-year lease durations are in very healthy spot rate spreads, will drive our run rate well into 2024 and 2025. In Q2, adjusted EBITDA margin, free cash flow margin, and return on invested capital, all expanded to record levels. I'll go into more detail on profitability drivers in a minute, but we see multiple levers that will support margins well into 2024, which in turn is allowing us to allocate capital with confidence.

We executed $70 million of tuck-in acquisitions in Q2 and expect that pace will increase through the end of the year. And we are using our growing surplus capital to repurchase shares with $891 million returned to shareholders in the last 12 months, and that represents over 9% of our outstanding share count over that period. Overall, our expectations for the year are unchanged with revenue and EBITDA up 12% and 19%, respectively, year-over-year at the midpoints. And as we approach the top end of our Investor Day operating ranges in 2023, our belief in the longer-term earnings potential in our platform is getting stronger.

Slide 22 lays out revenue and adjusted EBITDA for the quarter. The commercial KPIs that Brad detailed drove revenue up 11% year-over-year to $582 million. Obviously, that growth was strongest in our leasing revenues and down slightly in sales. Adjusted EBITDA increased 25% year-over-year to $261 million and we saw a normal sequential seasonal increase in our quarterly revenue and in line with our prior guidance. And in the bottom right

chart, you can see that 97% of our revenue is coming from our reoccurring leasing and services revenues. So with sales revenue down about $5 million year-over-year in the quarter, this is an extremely high-quality and predictable revenue mix.

It's worth spending a minute on our margin trajectory because it continues to be a source of upside in our performance and margins are benefiting from a combination of both short- and longer-term drivers. First, and as we've discussed on the last couple of calls, in the immediate term, work order activity is down relative to 2022 levels. And as a result, our variable rental costs are up only $5 million year-over-year. That increase is entirely due to inflation, and that inflationary impact will reduce as we progress through the year, which means leasing gross margins will have a natural tailwind as we head into 2024. Second, and again, as I mentioned last quarter, we are realizing very meaningful efficiencies in our modular refurbishment spend, having now operated in SAP for over 2 years. Our average cost per modular refurbishment was down approximately 20% year-over-year in Q2, and that is despite inflationary pressures. This is driving refurbishment CapEx down and free cash flow margin up to a record 27% in Q2. We believe these work order spend efficiencies are sustainable and we expect further relief from inflationary pressures as we progress into 2024, resulting in improved capital efficiency and cash conversion relative to the last few years. Third, we continue to see benefits of the improvements we made in 2022 to our logistics margins, which increased 230 basis points year-over-year. This has been driven primarily by pricing, which we expect to continue but we also see opportunity for cost efficiency as we consolidate our operations onto Field Service Lightning within our salesforce.com platform later this year, which will enable improved route management and then ultimately, optimization.

The market for sourcing drivers and trucks is also improving, which should allow us to in-source more transportation volume in our Modular segment which has been a challenge since 2020. So overall, we have multiple levers supporting gross profit margins, which expanded 370 basis points year-over-year and were up across all revenue lines and in both segments. And lastly, we're now getting very good leverage out of SG&A, which was down 260 basis points year-over-year to 23% of revenue. In absolute dollars, SG&A was down sequentially and flat year-over-year driven primarily by reduced variable compensation, again, relative to 2022, which was an unusually strong year for bonuses and commissions.

Looking forward, as we stabilize in our new consolidated CRM, we see significant opportunities to improve back office and workflow efficiency and expect this will be another source of operating leverage heading into 2024. All of this combined to drive adjusted EBITDA margin up 500 basis points year-over-year to 44.9% for the quarter, which is the top end of our Investor Day operating range. Flow-through of revenue growth to adjusted EBITDA of 88% and free cash flow margin of 27% are both outstanding. And we can look across all of the underlying key drivers and see benefits into 2024 and beyond. So margins are clearly an area where we see upside relative to our prior long-term guidance.

Page 23 provides more detail on cash flow, which is a highlight. Net cash provided by operating activities increased 7% year-over-year to $202 million. Keep in mind that these cash metrics are not adjusted for discontinued operations, so cash flows from our current operations are growing faster than 7% on a pro forma basis, and we expect that they will continue to expand in the second half of 2023. Net CapEx was $43 million, which is effectively at maintenance levels for the second quarter in a row. As I mentioned, moderating inflation, combined with improved work order efficiency are driving sustainable improvements in capital spend, whereas new fleet purchases are purely demand driven and won't be necessary given the fleet additions of last year. Steady top line growth, margin expansion, and

moderated CapEx resulted in company record quarterly free cash flow of $160 million and a 27% free cash flow margin. If annualized, this represents a $640 million free cash flow run rate, which gives us direct line of sight to the $650 million free cash flow target that we established at our 2021 Investor Day and over $3 of free cash flow per share based on today's run rate and share count of approximately 197 million shares. For the purposes of 2023, we see quarterly free cash flows in line with Q2 levels through the remainder of the year, which implies free cash flow for the year well in excess of $500 million and with a stronger run rate heading into 2024.

Turning to Page 24. Consistent with Q1, we are operating very comfortably at 3.0x net debt to adjusted EBITDA, which is at the bottom end of our target leverage range of 3.0x to 3.5x. We have over $1 billion of liquidity on our asset-backed revolver. So no near-term maturities of debt and a weighted average pretax interest rate of approximately 5.8%. So with these factors, accelerating free cash flow, and record return on invested capital, we are unconstrained from a capital allocation standpoint.

And Page 25 shows how our capital allocation framework and how we've allocated that capital over the last 12 months. Our capital allocation approach continues to be consistent with the framework that we shared at our 2021 Investor Day, which is shown on the left. As shown in the middle chart, we generated $1.6 billion of capital on a leverage-neutral basis over the last 12 months, inclusive of divestitures. Based on current guidance, net CapEx will decrease slightly as a percent of capital generated for the full year 2023 following the record levels in 2022. On the other hand, given our pipeline of tuck-in acquisition candidates, capital allocated to M&A should increase as we progress through the remainder of the year. That still leaves substantial surplus capital generated by the business which we are returning to shareholders via our share repurchase authorization, having reduced our economic share count by 9.1% over the last 12 months. Given the long-term earnings growth potential in our business, share repurchases are the right way to return capital and reinvesting in our business consistent with this framework is yet another lever within our control to deliver consistent compound returns over time.

Lastly, before turning it back to Brad and opening Q&A, page 26 shows our current guidance, which is unchanged from the prior quarter. All else equal, I would expect margins to continue trending stronger than we originally expected and with continued work order efficiencies also benefiting CapEx. But the underlying mix of price, volume, and value-added products is largely unchanged, which means our run-rate expectations heading into 2024 are also unchanged. Again, at the midpoints, revenue would be up 12% and EBITDA would be up 19% for the year with 250 basis points of margin expansion. And free cash flow should be well north of $500 million, up over 60% year-over-year, all of which sets up a strong trajectory for 2024.

As we progress from Q2 to Q3, I expect adjusted EBITDA to be flat or slightly down sequentially in Q3 with margins compressing sequentially, assuming variable rental costs continue to build through the seasonally stronger months, and then I would expect margins to expand again sequentially into Q4, which is almost always our most profitable seasonal quarter. Acquisitions, seasonal retail demand, variable leasing costs, and delivery and installation or sales revenues are really the only variables at this point that could take us higher or lower in those ranges as our leasing revenues are largely booked at this point in the year. That's the beauty of the predictability in our portfolio. It means we have a very high degree of confidence that we'll deliver the guidance and an outstanding year, and one which keeps us on track to achieve or exceed all of our longer-term operating targets. We've got a proven formula to drive sustainable growth and returns. We've got the best team in the business with a track record of consistent execution. And we've got a $1 billion portfolio of growth opportunities that will drive the business well beyond 2024, which is where we're focused.

With that, Brad, I'll hand it back to you.

Brad Soultz

Thanks, Tim. As always, thank you to our team and our customers for their continued support, and thank you to our shareholders for your continued trust with your capital. And thanks again to the team for the hard work to deliver not just the quarter, but as Tim referenced, continuing to drive towards 2024 and beyond. I wish all of you listening today continued safety and good health. This concludes our prepared remarks.

Operator, would you please open the line for questions?

Operator

Our first question comes from Tim Mulrooney with William Blair.

Tim Mulrooney – William Blair & Company, L.L.C.

Yes. My questions are on portable storage volumes down, I think, 6% primarily, I think, due to a pause on retail refurbishments. But I was curious if you were seeing softness anywhere else in any other markets as well or if that was the overwhelming primary driver of the decline was from the retail side?

Brad Soultz

Yes. Tim, that was the primary driver, but we are seeing the same kind of underlying core softening that you see in modular to storage as well.

Tim Mulrooney – William Blair & Company, L.L.C.

Okay. Got you. So are you expecting a similar, again, for portable storage volumes, a similar volume decline in the third and fourth quarters as well?

Brad Soultz

No, this is similar as we characterized in the last earnings call. First look at core demand, we expect to be down at the end of the year 2% to 3%. You'll see that most prevalently in modular and then we had the compounding effect in the second and third quarter of the store remodels, which was like 15,000 containers on a year-over-year decline.

Tim Mulrooney – William Blair & Company, L.L.C.

Okay. With these volumes coming down, is that also an indication that the spot rates are softening up right now as well? I'm just curious if like after 2 years of inflation and supply chain constraints, if you're seeing spot rates moving lower on a year-over-year basis.

Brad Soultz

No, we're really not seeing pressure on spot rates. I mean the market is very well organized. We're continuing to be frugal in terms of driving the incremental value with the product positioning and the logistics capability and the differentiated premium offering. So really not seeing any pressure on delivered spot rates. And as I mentioned in my prepared remarks, we're really not seeing much contribution from VAPS yet in storage, which will become more meaningful in 2024 and give us kind of that recipe that we've had in place for modular for 5 years, driving double-digit rate growth playing out in storage as well.

Operator

Our next question comes from Kevin McVeigh with Credit Suisse.

Kevin McVeigh – Credit Suisse

Tim framed really nicely kind of the variables on the full year guide. Do you know what to think about the dollar amount associated with them? And then just a quick follow-up. It's a lot of money, like right, I mean, $650 million is a lot of cash. Any thoughts, I know traditional capital allocation, but just any thoughts around maybe dividend or just affords a lot opportunity, particularly given where the balance sheet sits today.

Tim Boswell

Kevin, this is Tim. I'll start with the guidance and variables that could move us around within there. But the punchline is, as I said in my remarks, is the mix of volume, price, and value-added products really isn't any different than we anticipated coming out of the Q1 call which indicates relative stability across all of those key leasing KPIs. To Brad's point, we always, from the outset of the year, projected some year-over-year delivery declines from a core modular standpoint but that's more a function of 2022 being extremely robust rather than anything particularly different about 2023. And then you add the retail component on to that, which I think we've talked about at length right now. That retail piece is a source of potential upside as we go into Q4. As you know, we always service seasonal storage capacity for the big non-mall-based retailers going into the second half of Q3 and then into Q4. And we've obviously got more idle capacity this year with which to respond to that demand, and we're actively pursuing it.

Acquisitions, as always, in our guidance, are incremental. Variable cost progression is a factor, which should drive a temporary and sequential decline of EBITDA from Q2 to Q3, that's normal as volume activity picks up in the business. And then I'd expect those margins to pop back up probably north of Q2 levels when we get into Q4. So that's the sequential progression that we're expecting. And then the last variable that can move quickly is delivery and installation and sales revenues. Sales revenue is not a particular focus for us. We're 100% concentrated on driving that lease revenue run-rate at any point in time, and we still see a very attractive run-rate growth heading into 2024, which, again, is our primary focus and unchanged from the prior quarter.

As it relates to your questions around capital allocation, we haven't changed our framework. And frankly, we're very happy right now to deploy that surplus capital into the share repurchase as we look out 2, 3, 4 years in terms of where the business is going, that's absolutely an accretive source of return for our long-term shareholders over time, and we consider ourselves to be among those.

Your question around dividend is a good one. The stability of our cash flow streams absolutely supports that type of capital allocation. So I think it's more a question of when, not if, we start having that discussion with the Board. But sitting here today, obviously, the share repurchase is the right place to be putting our dollars.

Operator

Our next question comes from Faiza Alwy with Deutsche Bank.

Faiza Alwy – Deutsche Bank

I wanted to follow up on portable storage spot pricing. Based on the gap that you mentioned around 10%, it looks like there's some deterioration from 1Q into 2Q. But then I heard you say that there hasn't been deterioration. But can you just maybe clarify that for us? And I think historically, Tim, you've talked about how you've been a beneficiary of inflation. And now with the disinflation narrative taking place, I'm curious how you think about your ability to take pricing as we get into '24 and beyond.

Brad Soultz

Yes, this is Brad. I'll clarify the rate and then pass it over to Tim for the inflationary point. The delivered spot rates for containers continue to progress. That compression in the spread, if you will, is simply a function of faster convergence of the fleet. I think that spread was approaching modular back at the fourth quarter when we had the seasonal units out last year at record level prices, prices that were above the average of the core markets. So that spread compression, if you will, is not a function of declining growth in spot rates, rather quicker convergence for the average of the portfolio.

Tim Boswell

And Faiza, this is Tim. I think the disinflation narrative is exactly that, it's a narrative, not necessarily the reality, especially what you see across construction markets. I don't think you talk to a contractor out there that's talking about kind of disinflation across their business. So this is still an extremely healthy environment for both modular and container pricing. And then you add on some of the other tactical and strategic techniques that we use to drive product positioning, price segmentation, the value-added products and services offering, and then also benefiting from our differentiated logistics capabilities, especially on the storage side of the business where that's a differentiator. So no, pricing continues to be a highlight, and we don't see anything changing in that regard as we progress through the year.

Operator

Our next question comes from Andrew Wittmann with Baird.

Andrew Wittmann – Robert W. Baird & Co. Incorporated

I just wanted to clarify a response to a prior question. I think, Brad, you mentioned that core demand was down 2% or 3% was kind of the expectation for the year. I just want to make sure, was that comment specific to the Storage

segment? Or was that for the company overall? And could you comment on your updated expectations, if any, for core demand on the modular side of the business this year?

Brad Soultz

So the modular -- and let's wrap in the commercial and nonresi market, separating retail. As we've said on the last call, we expect it to be down 2% range at the end of the year. That same effect will impact the storage as well. The layover in storage is retail. And it's really -- there's a bifurcated effect in storage. You've got the remodels in the middle of the year, they largely didn't occur, and then you have your normal seasonal opportunity at the end of the year. The remodels didn't occur. The seasonal demand, as I mentioned in my prepared comments, has just started in terms of order flow. It's in line with our expectation in demand and timing, but it's very early in. So, I guess that's the bigger moving part, if you will, Andy, in storage as you look at year-end projections.

Andrew Wittmann – Robert W. Baird & Co. Incorporated

Yes. Got it. And then Tim, I just thought, just given that this has come up a couple of times this morning in some conversations, the quarter came in a little bit better than expected. Can you just talk about how that did or did not affect the way you approach guidance, the updated guidance here, which is, I guess, the same as last quarter.

Tim Boswell

Yes, like you said, a little bit better than expected, but we're not going to get too cute trying to manage guidance plus or minus 1% here. Very happy with the results in the quarter and encouraged by the margin trends in particular. Core leasing KPIs, very much in line with what we expected last quarter. But this is a business where we're looking out 2 or 3 years, and most of our time is spent focused on driving run-rates and things like that, that will push us over that type of time horizon. So very happy with the trajectory of the business, implied run-rate going into next year, it sets up a very good 2024. And frankly, I can't find any real red flags across our core KPIs that would cause me concern about executing any of those long-term targets.

Operator

Our next question comes from Scott Schneeberger with Oppenheimer.

Scott Schneeberger – Oppenheimer & Co. Inc.

So a lot of questions with regard to just consideration for demand across the two main segments. Could you all please elaborate on -- it sounds like just in general, is core demand of about down 2% to 3% for the year, slightly softer than where you were looking at the year at the beginning? Could you talk about nonres, reshoring, CHIPS and Science Act, infrastructure bill, Inflation Reduction Act, what you're seeing across all these that would pose any risk or upside to that down 2% to 3% in the back half and going into 2024?

Brad Soultz

Yes, Scott. Again, this is a reminder, these are 3-year lease durations, so units on rent move slowly. I would recall in my comments in the prepared remarks, our second quarter North American modular quote rates were modestly up over prior year. And prior year was at record levels. So there's no crisis or issue here. Now objectively, construction nonresi starts in the first half, whether you look at dollars or square foot, were down, right? ABI went through a soft period, it's now stabilized. So there's no new news here. This is what we alluded to when we issued guidance, we kind of reaffirmed in the first quarter, and that's really where we're sitting here today. So, I think as we look forward into the second half of the year and certainly into 2024, we're extremely excited about the potential of the onshoring, reshoring, infrastructure stimulus, and such. And it's not the fact that we're sitting here waiting for something to materialize in D.C., it's already happening, right? We're bidding, we're winning these projects. They're super exciting, and we are extremely uniquely positioned to take advantage of the opportunity and service the customers' needs in these cases.

Scott Schneeberger – Oppenheimer & Co. Inc.

Great. And then my second question is a two-parter with regard to VAPS. Your European peer talks about its VAPS penetration that's around greater than 60%. Where would you say -- this is specifically about modular, your VAPS penetration is, is the first part of the question. The second part is, in the quarter, the VAPS average monthly rental rate was up 13% year-over-year, but the LTM delivered rate was down 1% year-over-year. Are you tapping out on the VAPS story is where I'm going with this, if you could just describe that dynamic in the quarter? And is there any concern that maybe modular is getting long in the tooth in the VAPS story, you've maintained the $650. Is that going to come from portable now? Or are we still feeling comfortable on modular?

Tim Boswell

Scott, it's Tim. I'll attempt to answer at least the first part regarding our European peer. But I think the best way to look at penetration is VAPS revenue relative to kind of the core unit leasing revenue. And if you look at our delivered rate of, call it $471 over the last 12 months in a spot rate that's north of $1,000 per unit for modular, you're easily approaching that 50% range. If you wanted to look at penetration just in terms of the relative dollar contribution, I think that's probably the best way to do it. So we're really just focused on that dollar contribution at the end of the day. There is some -- well, the LTM VAPS delivered rate has flattened out. I think you also saw a commensurate pickup in core unit lease pricing in modular and that's -- there is some fungibility is the wrong word between those two. But in the core unit pricing standpoint, for example, we're getting surcharges now for things like restrooms and sanitation, which are value-added in their own right, although not going to be impacting the LTM delivered metric. And as we look at just the core VAPS offering across the salesforce, there's still a very wide dispersion of performance around that, with top performers well in excess of the numbers that we're reporting here today. That's been the case forever, and that's the best practice sharing and coaching that we use to drive this over time. And this has been going on now for well over 10 years. And no change in terms of our expectations of pushing the salesforce to $650 per unit over time.

Operator

Our next question comes from Steven Ramsey with Thompson Research.

Steven Ramsey – Thompson Research Group, LLC

Maybe to start with the CapEx efficiencies you have gotten so far in the modular refurbishment efforts, was this part of the $500 million target or the 3- to 5-year target of well over $500 million? And is this enough to move that range upward as you keep building on these efficiencies?

Tim Boswell

Steven, this is Tim. That's a good question. Because as we go back to think about the Investor Day framework that we laid out, we presented a bridge to $650 million of free cash flow. And the CapEx assumption in that bridge was circa $275 million. That $275 million probably wouldn't have had an assumption around the inflation that we incurred through the course of 2022, nor would it have assumed meaningful refurbishment efficiencies. So I think there's probably some natural offset there, such that I'm actually very comfortable with the $275 million that we put in that bridge. And in fact, it's the midpoint of our guidance this year not coincidentally. So I don't know that I'd point to too much change there other than it is definitely an improvement over the 2022 run-rate that we're on and gives me confidence that we can keep it in the range that we had advertised as we head into 2024 and beyond.

Steven Ramsey – Thompson Research Group, LLC

Okay. Interesting. That's great. And then on storage VAPS, I realize it's not a small – it's a tiny part of the reality for current financial results. But is this part of conversations with retail customers for Q4? And is this part of conversations with customers on quoting activity for projects that are set to start over the next 12 months?

Tim Boswell

100% on storage VAPS. And the nature of these things is they do take a little while to build. But as the portfolio churns, you start to get a compounding contribution from these types of things. And I won't say that VAPS in the Storage segment are insignificant. If you include the ground level office fleet, for example, we'll be pushing north of $90 million of revenue this year from value-added products and associated services in storage. The container portion of that is just now beginning to build. And if you look over like the last 6 months or so, you're delivering the average container with north of $30 per unit per month of value-added products and services, which translates to probably a $50 million run-rate as you go into 2024. And that's before any contribution from PRORACK, right? So this is playing out frankly, better than we expected back at Investor Day.

And the other thing, just to follow up on Scott's question, as you just think about what does all this mean? If we just hold value-added products penetration where it is today, across all of these products, you're talking about a $200 million revenue convergence opportunity that is yet to flow through our P&L. You hold pricing where it is today, there's about another $200 million convergence opportunity that is yet to flow through the P&L. So these are things we're very excited about. We're continuing to push the spot rate side of things. We absolutely have a value-added

products penetration opportunity on storage that we're seeing, which is becoming part of the customer conversation. And to Scott's question a minute ago, no concerns about getting back to that $600 per unit trajectory on modular.

Operator

Our next question comes from Philip Ng with Jefferies.

Philip Ng – Jefferies LLC

Congrats on another strong quarter. The market is obviously nervous about new nonres activity slowing down and you called out ABI as well, but you also highlighted the strength on the infrastructure side and some of these mega projects. So when we think about these cross currents, looking out to 2024, how should we think about what that translates to volumes next year? And then any color on how your bidding activity is progressing so far?

Brad Soultz

Yes. As I referenced, our quoting activity in the second quarter in NA Modular was up modestly over prior year. That's phenomenal, especially considering how strong 2022 was. As far as like cross currents, the fact that the ABI has stabilized into neutral to positive territory, right, following 2 quarters of contracting territory, that's very supportive of a 2024 outlook. So I think we've probably seen, if the ABI continues to remain strong, we see kind of core markets stable and recovering and you basically pour jet fuel on with infrastructure, onshoring, reshoring, and everything else that's already beginning to play out today.

Philip Ng – Jefferies LLC

So it sounds like, Brad, at this juncture, you're [preaching] your business is pretty short cycle. You're not expecting volumes to be down big next year. It sounds like it might have some upside next year. So that's pretty encouraging. And I guess switching gears, a question for Tim. I think you went out of the way to kind of highlight all the good stuff you guys are doing on the cost and execution side and the inflation coming down and then still pretty good momentum on pricing. What kind of volumes decline would you need to see for margins not to be up next year? Because it sounds like you got a lot of runway on the margin side of things for 2024.

Tim Boswell

Yes. I mean I haven't done that exact math, Phil, that would be hard to get to. Given I just said that you've got almost $400 million of revenue convergence opportunity across pricing and value-added products. And rough math is you get roughly 1/3 of that flowing through a year, just based on our 3-year lease durations, and the cost efficiency opportunities on top of that. I feel very good about margins going into 2024. And I think around this time last year, I said I felt very good about margins going into 2023, and we just popped 500 basis points in Q2, and we'll be up at least 250 basis points for the year. So this is a business where you get those structural revenue growth opportunities flowing consistently and predictably through the portfolio as it churns. There's operating leverage in the business and quite a bit of discretion over things like variable costs and CapEx, which I don't know, make me very happy about the margin trajectory.

Operator

Our next question comes from Manav Patnaik with Barclays.

Ronan Kennedy – Barclays Bank PLC

This is Ronan Kennedy on for Manav. On the M&A, with the $80 million of tuck-in acquisitions last quarter, $70 million this, what is the expected contribution for full year '23? And then can you remind us about the acquisition financial profile in terms of the multiple, the synergy unlocking value enhancement, economic return profile, et cetera. And on the return profile, the unit level cumulative cash flow, I don't think those have changed in the slides, in the presentation. Have there been changes to the acquisition costs, the maintenance, as a result of efficiencies, etcetera?

Tim Boswell

Ronan, this is Tim. I'll start with your questions around acquisition contribution. And I think the best way to -- we called out that there is roughly $17 million of revenue flowing into the Q2 numbers from acquisitions in the last 12 months. You can assume that, that annualized run rate is a little bit higher than the $17 million because of some of those occurred during the course of Q2. So call it $20 million annualized that, you're at [$80 million,] put mid- to high 30s margin on that, and you've got an idea of the annualized EBITDA that's been acquired. And then if you compare that to the LTM acquisitions of $266 million in the last 12 months, you'll get about an 8.5x implied enterprise multiple at which we purchased those businesses. Fair to assume over a 12-month period that we get some synergy uplift, primarily from cost and just operating those assets and branches consistent with the rest of our branch network. And then over time, as the portfolio churns, we get the benefits of pricing uplift and value-added products uplift depending on the specific asset class that we're talking about. So the tuck-in strategy is highly programmatic. We've got a team that meets weekly to manage a pretty exhaustive pipeline of opportunities, both early stage and recently integrated. So it is a repeatable process and core competency that we've developed since the completion of the Mobile Mini integration. And I'd expect that our investments there probably pick up a little bit as we close out 2023 and that continues to be part of our growth algorithm as we go into future periods. So very happy with that.

And we haven't been in the habit of updating kind of the unit economics slide every quarter. We kind of revisit it once a year based on material changes. So yes, we're seeing some improvements in that kind of refurbishment cost on modular in the latter 1/3 of the unit's life. And in terms of unit sourcing costs relative to spot rates and things like that, I still think pointing to roughly a 40-48-month cash-on-cash payback on modular and 36-month cash-on-cash payback on containers. Then accelerate those returns with value-added products and services. Conceptually, that's still the right way to think about the unit economics in our business.

Ronan Kennedy – Barclays Bank PLC

Appreciate it. And then a follow-up to a prior question that was asked on the CapEx efficiencies in the refurbs. Can I just confirm for the remainder of the year, the expected sequential progression on CapEx and free cash flow? And then when do you expect CapEx to kind of reflect or inflect to bring back some of the growth? I know it's a function of the 90-day capital planning, but what are the expectations for that?

Tim Boswell

Yes, I'd expect that CapEx increases sequentially along with our other variable costs in the P&L into Q3. And then a little more -- we haven't baked Q4 yet because we don't have a very long -- we have no long-term supply commitments in this business. We can actually be very reactive based on demand. But I do expect CapEx to increase sequentially as we go from Q2 into Q3. And then in terms of kind of more substantial fleet investment, there may be some kind of niche categories that we have in mind that could come to play in Q4 as we head into 2024. But in terms of our core modular and storage fleet investments, we typically wouldn't be ramping those up to support core demand growth until we get into the second half of Q1 heading into Q2 of next year, and that will obviously be part of our annual guidance for 2024. But to the question earlier, if I was starting to think about what's the number that I center around, it would be that $275 [million] number that we centered around in the Investor Day bridges that took us to the $650 million free cash flow range.

Ronan Kennedy – Barclays Bank PLC

Sorry, free cash flow progression for Q3 and Q4, if I could please confirm that?

Tim Boswell

Yes, it should be roughly in line with where we left coming out of Q2, maybe it dips a bit based on increased capital spend going into Q3. There's also going to be some offsetting growth there. And then typically, CapEx would go down a bit and margins would go up a bit in Q4 and free cash flow historically has been highest in Q4. So that would be probably a good base case to think about, but it will be demand driven and largely based on any CapEx fluctuation.

Operator

Our next question comes from Brent Thielman with D.A. Davidson.

Brent Thielman – D.A. Davidson & Co.

Great. Tim, just the consideration for margin expansion into the fourth quarter, hoping just to clarify to what degree is the seasonal uptick in storage critical to that versus the other variables and drivers? In other words, would you still see that margin enhancement even if the seasonal activity in storage is possibly less than what you anticipate today?

Tim Boswell

Yes, Brent, it's absolutely the latter. The seasonal doesn't really impact my thinking at all as I give that guidance. It's really driven by the fact that repair and maintenance activity typically slows down in Q4. But as you know, our lease revenues just don't change very much, right? So what I would expect sequentially coming out of Q2 is maybe we get up to 200 basis points of margin contraction as we go into Q3. That will be driven by variable costs ramping up in the business. And then you could get maybe 400 points of sequential expansion going from Q3 into Q4. And that's, again, just driven by variable cost fluctuation in the business. Give me some latitude on the magnitude of those changes, of course. But order of magnitude, that's, I think, how we finish the year and that puts you at a kind of record

margin heading into 2024 which, again, is why I've got a high degree of confidence on that. And it's not driven really at all by the seasonal business.

Brent Thielman – D.A. Davidson & Co.

Got it. Okay. I appreciate that. And then just could you guys speak to the supply dynamics in the industry for both modular and storage? I recall that being constrained in recent years. I presume you've always been prioritized among your vendors. But to what degree do you see availability today for the industry versus a few years ago? Is it a greater circulation out there in terms of assets? If you could comment on that, that would be helpful.

Tim Boswell

Brent, it's Tim. I haven't really seen any material change. I'll start on the modular side of the business, and to the extent we're sourcing traditional product domestically, which is what virtually all of our competitors would be doing, we'd be sourcing from a network of 20-plus, pretty much local manufacturers of modular buildings. At most, maybe 10% of the manufacturer's business will be focused on rental fleet. The primary focus would be permanent modular construction projects, which is not an area where we care to participate. So it is a fairly limited domestic supply base. And I think because of that, you haven't seen procurement costs really come down at all over the course of the last 12 months, which, again, to one of the earlier questions around deflation, I think that's more a narrative than it is a reality in our business, right? Any new capacity coming into the market today, especially on modular is at a much higher cost basis than the industry would have been managing historically. And frankly, we have some prospective sellers in our acquisition pipeline who are talking to us precisely because of that reason. Acquisition costs or procurement costs are up, capital costs are up, which makes it more difficult for a smaller competitor to grow their business and enhances our competitive position in the market, given our available capacity.

A little bit different on the storage side. Those container prices can fluctuate to an extent with the capacity in the maritime shipping world. But it's quite another question to have that capacity filter its way into all of our diverse 300 local markets where we're competing every day. So we just don't see that happening or impacting supply availability to a material degree, or frankly, pricing to a material degree.

Operator

Our next question comes from Sean Wondrack with Deutsche Bank.

Sean Wondrack – Deutsche Bank

Great job on progressing on your goals from Investor Day. It's great to see. And when you think about some of these larger projects, the mega projects that continues to sort of dominate the headlines. When you think about the profile on that project, is that going to have like a different mix element than what you've typically seen, given that they're sort of becoming a bigger maybe part of the mix there? Can you maybe talk about sort of the average duration of these things and how they compare to your other contracts?

Tim Boswell

Yes, Sean, it's a good question. I think there is absolutely going to be a mix shift in the overall balance of non-residential construction activity moving towards these types of projects. And I think it's still very early innings. When we look at over 100 of these mega projects kind of in our CRM today, the vast majority haven't even started yet, right? And we do have a disproportionately high win rate on those projects. And that is in part because they are larger, longer duration, more employees on site, more likely to need more sophisticated, complex, higher square footage turnkey solutions, which is our sweet spot. That's where we've got the strongest competitive positioning in the market, and we're the only pure-play space provider that can cross-sell across all of our different capabilities into those opportunities. If you look at projects that have been announced or awarded related to the infrastructure bill, the vast majority of those haven't started yet either. So, Brad talked about nonres square footage down in the first half of the year, that's really before the impact, I believe, of the majority of these reshoring and infrastructure-related projects, which is one of the reasons we feel pretty good about the future in 2024 on the volume side and are disproportionately strong competitive positioning given that mix change.

Sean Wondrack – Deutsche Bank

Right. And then when you just think about -- does it strike as a typical contract where it's roughly a year duration and then there are sort of escalators as you move forward? Or would it be like a 3-year project, maybe a little bit lower margin, I'm just kind of curious how that sort of looks from a high level.

Tim Boswell

I wouldn't characterize a 3-year project as being lower margin because you've got very little variable costs associated with that contract over the course of 3 years. So absolutely, these, all else equal, should skew longer duration relative to our -- what has now become a 13-month, I think, minimum contractual term. We have seen some increases in term partly due to project delays. But I think part due to the mix of our business and being positioned more towards these larger scale opportunities. So yes, I would expect longer contract duration on -- it tends to correlate with project size. And yes.

Sean Wondrack – Deutsche Bank

Got it. That's very, very helpful. And then if I could sneak one more in. You have the 6.125% notes due 2025 coming due in just short of 2 years. I was curious, are you considering doing something with them? And then also, do you have the flexibility to repay them with your revolver? Should you desire to do that?

Tim Boswell

Yes, 100%. That's what the revolver is there for. We could refinance them into the Revolver tomorrow if we if we so choose. And then, as you know, we've been a repeat issuer in the high-yield market. There's no urgency to frankly do anything about the 6.125% notes right now just given where short-term benchmark rates have moved. So we're quite happy with them. We've always got the availability to refinance them into the ABL, and we can be opportunistic as it relates to activity in the high-yield market. You'll be well aware, we got upgraded recently by S&P. So I think we're

now 2 notches closer to the United States credit profile. So very happy with the progression of our credit metrics and frankly, the flexibility in our debt structure.

Operator

We have now reached the end of today's call. I will now turn the call back over to Nick.

Nick Girardi

Thanks, Amy. Thank you all for your interest in WillScot Mobile Mini. If you have additional questions after today's call, please contact me.

Operator

Thank you. Ladies and gentlemen, this concludes today's conference. You may now disconnect.